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FEDERAL COMMUNICATIONS COMMISSION
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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of

Implementation of the
Cable Television Consumer
Protection and Competition
Act of 1992

Rate Regulation

MM Docket No. 92-266

COMMENTS OF THE COMMUNITY ANTENNA TELEVISION
ASSOCIATION, INC.

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SUMMARY

1. The issues raised in the Commission's Further Notice can be simply categorized. Two, the treatment of addition or deletion of channels under the benchmark system, and whether systems can choose one form of regulation (benchmark v. cost-of-service) for one tier of service and another for a different tier of service, concern how rates are regulated. The other two issues deal with the treatment of system upgrades.

2. CATA maintains that problems associated with the addition or deletion of channels under the Commission's tentative proposal can be significantly eliminated if the Commission will abandon its adherence to tier neutrality. Whatever useful function tier neutrality has served in arriving at a benchmark system for present cable tier offerings, it is apparent that it will produce anomalous and inequitable results if it is applied on a going forward basis. A system for determining per-channel charges that account for the programming costs of additional channels must be cost-based and, reasonably, should be applied only to the tier to which the channels will be added. Further, new per-channel prices arrived at for one tier, should be independent of prices on other tiers.

3. Similarly, unburdened by the albatross of tier neutrality and the fear that per-channel prices might differ for

different tiers of service, the Commission can sensibly decide to permit systems to choose the form of rate regulation most appropriate to a given tier. This would potentially spare local franchising authorities and systems the necessity of having to engage in costly and unnecessary cost-of-service proceedings.

4. CATA agrees with the Commission's tentative conclusions that systems that initiated upgrades shortly before rate regulation should be permitted (at least) to bring below benchmark rates up to the benchmark level in order to account for upgrade costs. We would go further. Systems should be able to raise rates to the benchmark level to account for such costs regardless of when an upgrade may have been initiated, and, indeed, this approach should apply to future upgrades as well.

5. Finally, CATA agrees with the Commission that the cost of upgrades required by local franchising authorities be given external cost treatment. We disagree with the option of leaving to local franchising authorities decisions as to the manner in which rates would be adjusted to reflect upgrade costs. If local authorities are to exercise such authority it should only be under specific guidelines from the Commission.

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COMMENTS OF THE COMMUNITY ANTENNA TELEVISION
ASSOCIATION, INC.

1. The Community Antenna Television Association, Inc., ("CATA"), hereby files comments in the above-captioned proceeding. CATA is a trade association representing owners and operators of cable television systems serving approximately 80 percent of the nation's more than 60 million cable television subscribers. CATA files these comments on behalf of its members who will be directly affected by the Commission's action.

2. Addition or Deletion of Channels. The Commission has proposed a method within its benchmark process of adjusting per channel rates upon the addition or deletion of channels. It is the Commission's stated intent to allow systems to recover program costs, and create an incentive to add channels that contain higher quality programming. CATA believes that the Commission's proposal will result in per-channel rates wholly

inadequate to support the addition of new channels.

3. The fundamental problem is that, because the Commission appears wedded to its present benchmark structure, it would average programming costs over all cable channels, not merely the channels on the tier to which the additional channels are added. Obviously, this reduces the resulting per channel charge which, when applied to the tier to which channels are added, results in an inadequate return. Moreover, if the resulting per channel charge for a tier to which channels are added, is similarly used for other tiers - as the concept of tier neutrality would suggest - truly anomalous situations will result. As the Commission is aware, depending on numbers of channels in each tier, old programming costs, and new programming costs, rates charged for tiers to which channels are not being added could go up or down. The result would be a rate change for the basic tier, for instance, without any change in channel offering. CATA urges the Commission to make clear that such a result will not be permitted to occur.

4. Under the Commission's proposal, systems with high existing average programming costs are penalized. The higher the costs, the less the resulting per-channel charge when channels with additional programming costs are added. It is certainly not intuitive that this should be the result of already paying higher programming costs. The effect, however, is that smaller systems

that traditionally have higher programming costs would be at a disadvantage. It is also noted that while the revenues resulting from the addition of more costly channels would be higher under the Commission's proposal (although still inadequate), revenues from the addition of a low cost channel can be negligible.

5. The Commission's formula is also deficient because it does not properly account for the cost of adding channels. The Commission intends the formula to work for systems with existing channel capacity that do not require re-builds in order to add channels. But channel activation depends on more than just capacity. For every channel added, a system must buy a signal processor. Typically, signal processors cost around \$2500. In addition, for satellite channels it is necessary to buy satellite receivers at a similar cost. Thus, in most cases, the addition of a channel will cost a cable system approximately \$5000. This is a real cost that must be recouped, but the Commission's proposal makes no provision for it. In addition, the start-up of any new cable channel must be accompanied by promotion. Promotional expenses are as much a cost to the system as program costs. Again, the Commission's formula does not address them. Finally, it must be noted once more that, as many commenters have pointed out, the Commission's benchmarks do not assure profitability. Although the Commission continues to rely on the assumption that the competitive systems it studied in order to develop the benchmarks must surely have been profitable, it is

clear that for many of them this was not the case. Thus, any formula designed to encourage addition of channels, particularly higher quality channels must be designed to include some margin of profit to the cable operator.

6. CATA believes that the Commission's goals are laudable and we make the following recommendations to help the Commission achieve them. First, as we note below, it is necessary to abandon tier neutrality. Tier neutrality has served its purpose. Even given the complications of determining benchmark rates, adopting the concept of tier neutrality probably made it easier. Tier neutrality enabled systems more easily to use the benchmark system to adjust their rates during the rate freeze, thus solving problems of cross-subsidization of tiers that would have been much more difficult otherwise. Moreover, if it was the Commission's intention to adopt a rate structure that assured a general reduction of cable rates nationwide, adopting a tier neutral benchmark system certainly helped to achieve this goal.

7. The fact remains, however, that the issue now concerns "going forward." Given the rates established by the Commission, it is necessary to move on. Assuming a desire to have a cost-based rate structure, tier neutrality can only be seen as an impediment. It certainly makes no sense to determine rates for one tier, based on costs peculiar to the offerings on that tier, and then similarly adjust per-channel charges on unaffected

tiers. The result of such a process will be seen as mischief. If subscribers are complaining now simply because there has been an adjustment between tiers during the rate freeze, one can only imagine the dissatisfaction should rates go up in the absence of additional service or channels simply because the Commission's processes permit it. And if it was difficult to explain that recent rate increases resulted from an elimination of cross-subsidization between tiers, explaining the esoterica associated with tier neutrality will be impossible.

8. If we are attempting to determine an appropriate per-channel charge when channels with programming costs are added or deleted from one tier, then it would only seem reasonable to look to that tier only. CATA believes, for instance, that one of various approaches that might be taken to improve the Commission's proposal, would be to average existing and additional programming costs only over channels on a tier to which additional channels are to be added or channels are to be deleted. The result would be closer to cost-based pricing for that tier. Another approach might be to simply average the new programming costs over the channels on the tier to which additional channels are to be added and account for whatever economies of scale are enjoyed with a greater number of channels by adopting a simple adjustment factor. These and similar proposals would more adequately reflect system cost for a given tier of service, and can be adopted if the Commission will

discontinue its adherence to tier neutrality.

9. Upgrades Initiated Shortly Before Regulation. CATA believes that systems be permitted to charge up to the benchmark rate to reflect the costs of system upgrades that were begun in advance of the passage of the Cable Act of 1992. The Commission presumes that a below benchmark rate reflects a cable operator's satisfaction with revenue levels. CATA and others have taken issue with this view. The presumption fails entirely, however, in cases where the operator did not even have the opportunity to account for a re-build in its rate structure. It is clear that such an operator will have to increase revenues to account for the costs of rebuilds. In cases where coming up to the benchmark level is satisfactory to the operator and cost-of-service proceedings can be avoided, then by all means the Commission should extend the option of increasing rates to the benchmark level. Theoretically, of course, it is possible that a cost-of-service proceeding might yield a rate between the current below-benchmark rate and a rate at the benchmark. This eventuality, however, would seem slight, and any concern in this regard should be more than outweighed by the simplicity and administrative advantage of avoiding a cost-of-service proceeding. The option of raising rates to the benchmark level to account for rebuilds and upgrades would be of particular benefit to smaller systems who may not be able to afford the expense associated with cost-of-service proceedings.

10. This same logic, of course, applies for systems charging below benchmark levels who may initiate an upgrade after rate regulation. It is not reasonable to assume that a cable operator will embark on costly upgrades merely to raise rates to the benchmark level. System upgrades occur either because aging plant must be replaced or because an operator wishes to increase its level of service. In any event, the Commission recognizes that the costs associated with upgrades must be recovered. In many cases, recovery of costs will require cost-of-service proceedings. But where an operator believes this can be accomplished merely by raising rates to the benchmark level the Commission should not adopt policies that would prevent such a simple accommodation.

11. CATA presumes that where a system is currently charging below benchmark rates and undertakes an upgrade for the purpose of adding channels of programming, the Commission would permit the system to come up to the benchmark for its current channel offering in order to recover its upgrade costs, and then apply whatever scheme the Commission selects in order to account for the addition of channels. To the extent both mechanisms are straightforward, and easy to apply, the Commission, local franchising authorities and many cable systems might be able to avoid time consuming administrative proceedings.

12. Operator Discretion to Select Benchmarking or Cost-of-Service for Different Regulated Tiers. The Commission has proposed that cable operators be required to use the same rate setting mechanism - benchmarks or cost-of-service - to determine the rates for all tiers of regulated service. After setting forth in paragraph 147 of the Further Notice five perfectly valid reasons not to take such action, the Commission nonetheless concludes that "out of an abundance of caution" it must propose that operators choosing the cost-of-service approach on one tier must engage in the same costly process on other tiers. Citing the concerns of NATOA, the Commission states that such a requirement "would prevent cable operators from 'gaming,' i.e., deciding whether it would be advantageous to submit a cost-of-service showing on one tier and a benchmark analysis on another."

13. First, it must be noted that it is not axiomatic that cable operators be prevented from making advantageous business decisions. It is hardly surprising that NATOA would consider such a process "gaming," but it is shocking that the Commission would agree. If, after a major re-build of a system, and after attributing the appropriate costs to the basic tier, it appears that a benchmark rate suffices, what useful public purpose would be served by requiring the operator and its local franchising authorities to embark on a cost-of-service proceeding? The Commission's answer to this seems to be that there is a risk that a cable operator would have a basic tier made up of lower cost

channels (which is, of course, what basic tiers are and will continue to be, regardless of the Commission's decision in this proceeding) and an enhanced tier for higher cost channels. And because the benchmarks are really averaged rates, using the benchmark approach for the basic tier might produce a rate exceeding the costs. At the same time the operator would be able to charge higher than benchmark rates for the more costly upper tier. "This result," the Commission explains, " would seriously undermine the rate averaging and tier neutrality concepts built into the benchmark approach by allowing operators to apply the average per channel rates derived from the benchmark formula only to certain tiers." CATA respectfully submits that the Commission has genuflected once too often at the altar of tier neutrality. The Commission itself realizes that unwavering adherence to tier neutrality will produce anomalous results. As a consequence it has been forced to request comment on such issues as whether cost-of service proceedings at the local level and the federal level might be consolidated, whether one regulatory body should give weight to the cost-of-service deliberations of the other and, if so, how much, or if the opinion of one regulatory body should be controlling, whether systems might be permitted to switch from one form of regulation to the other and, if so, at what intervals. Is the Commission prepared to abandon the legislatively mandated dichotomy between local and federal regulation of cable tiers in order to preserve tier neutrality? Based on the clear legislative language, can it?

14. As the Commission stated, one party to this proceeding has already pointed out that, depending on the date that different tiers of service become subject to regulation, there will be different per-channel charges. Even if cost-of-service proceedings are held for all tiers of service on a system, it is likely that different regulatory bodies, examining different costs for each tier, will arrive at different per channel charges. And in many cases where, in anticipation of rate regulation, systems have already adjusted their basic tier rates to the benchmark, local franchising authorities will not bother to begin rate proceedings at all, but the systems may well choose to justify upper tier rates based on costs. Thus, over time, the concept of tier neutrality will lose significance. But decisions made now in aid of preserving tier neutrality will have lasting effect. CATA urges therefore that the Commission take the longer view. One of the stated reasons for devising a regulatory scheme based on tier neutrality was simplicity of administration. It would be a perverse twist if, in order to preserve tier neutrality, rate regulation became even more complicated.

15. Cost of Upgrades Required by Local Franchising Authorities. CATA believes that system upgrades required by franchising authorities be given external cost treatment. The issue, as the Commission has recognized, is how this is to be done. Neither of the two alternatives suggested by the Commission is wholly satisfactory. First, it is not clear what

the Commission intended when it proposed that the cost of upgrades might be governed by standards adopted in the cost-of-service proceeding. In that proceeding the Commission addressed itself to the possibility of using a streamlined cost-of-service approach to deal with upgrades or re-builds. CATA supported such an idea as one alternative, among others, that should be available to operators. But until details of a streamlined approach to upgrades are available it is difficult to comment. There was little other discussion of upgrades or re-builds in the cost-of-service proceeding.

16. Leaving the question of factoring system upgrade costs into rate setting to the local franchising authorities without considerable guidance creates a recipe for confusion. This would especially be the case for single systems serving more than one franchise area. Disparate and uneven treatment of the upgrade issue would be bound to cause uncertainty, increase investment risk, and delay a system's ability to offer new services to consumers. The regulatory scheme adopted by Congress and the Commission leaves rate regulation of basic tier services to local franchising authorities. But just as the Commission provided the benchmark system that local franchising authorities are bound by, so too should the Commission adopt guidelines to govern the way in which rates can be adjusted to account for the costs of re-building.

17. Conclusion. CATA urges the Commission to give tier neutrality a long look and then, however reluctantly, turn away. Having done so, it will then be possible to adopt a more accurate cost-based approach to the addition or deletion of channels for individual tiers of service. Operators would be able to choose cost-of-service regulation in cases where tier costs make that approach seem warranted, and the benchmark process for other tiers. CATA believes that the Commission must also simplify its processes by permitting systems with below benchmark rates to raise rates to the benchmark level (if that is deemed satisfactory to the system) to account for system upgrades regardless of when the upgrade was commenced. Finally, CATA agrees with the Commission's tentative view that the costs of upgrades required by franchising authorities be given external cost treatment. Such a decision should be accompanied by Commission guidelines concerning the method for rate adjustment.

Respectfully submitted,

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